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No. 97-546

Supreme Court, U.S.
FILED
NOV 10 1997
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

FIGTER LIMITED,

Petitioner,

vs.

TEACHERS INSURANCE AND ANNUITY ASSOCIATION OF AMERICA,

Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITIONER'S REPLY BRIEF

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12pp

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PETITIONER'S REPLY BRIEF

INTRODUCTION

Petitioner Figter Limited ("Figter") respectfully submits this Reply Brief in further support of its Petition for a Writ of Certiorari and in reply to the Opposition to the Petition filed by Respondent Teachers Insurance and Annuity Association of America ("TIAA"). The Petition arises in the context of Petitioner Figter's Chapter 11 bankruptcy case and from the purchases by Respondent TIAA of twenty-one claims in the unsecured class in which it was previously not a member. Respondent has admitted that its purpose in purchasing the unsecured claims was to block the Petitioner's plan of reorganization. The Court of Appeals for the Ninth Circuit affirmed the decisions of the District and Bankruptcy Courts below holding that the purchased claims would not be designated as being purchased in bad faith and that Respondent could cast one vote for each of the purchased claims. The Petitioner seeks review of the Ninth Circuit Opinion not only because such decision conflicts with applicable Supreme Court precedent, but because the decision below raises important Federal questions regarding the purpose, policies and operation of the Bankruptcy Code and the impact on Chapter 11 debtors and their ability to reorganize.

In the Petition, the Petitioner demonstrated that, contrary to arguments set forth in Respondent's Opposition Brief, that the opinion below ***does*** conflict with applicable Supreme Court precedent (Petition at 6-8) and that the Federal questions raised ***are*** important ones (Petition at 8-12). The Petition should be granted so that this Court may settle these important Federal questions.

1. The Ninth Circuit Opinion Decided Important Questions of Federal Law Which Should Be Settled by this Court.

In its Opposition, Respondent asserts that the Ninth Circuit did not decide an important Federal question. (Resp. Br. at 10). Respondent does not, however, discuss why the issues determined by the Court of Appeals are not important questions of Federal law. Respondent argues that the Bankruptcy Code "represents Congress' delicate balance of the rights of debtors and the rights of creditors" (Resp. Br. at 10), but does not explain what that balance is and what impact the Ninth Circuit's Opinion has on such "balance." More significantly, Respondent failed to address any of the Petitioner's arguments in the Petition regarding the impact and effect of the Ninth Circuit Opinion on the Bankruptcy Code and its purposes, on Chapter 11 debtors and on single asset real estate cases.

As discussed in the Petition, the Ninth Circuit Opinion would permit any secured creditor in a Chapter 11 case to purchase a blocking position so as to prevent a Chapter 11 debtor from meeting the requirements of Section 1129 of the Bankruptcy Code and thereby to have a plan of reorganization confirmed. If the Federal courts were to sanction such activity, it would have the practical and adverse effect of preventing any reorganization in a Chapter 11 case where the secured creditor decided to engage in such tactics. The impact of the Ninth Circuit Opinion would thus not be limited to the particular facts of this case. Its impact would be seen in variety of circumstances, involving any Chapter 11 debtor and a secured creditor or creditors in such a case. The consequence of the Ninth Circuit Opinion would thus severely undermine the operation and purposes of the Code.

To allow the purchase of a blocking position by a fully-secured creditor, especially where it previously held no unsecured claim which it could argue it was trying to protect,

would, in effect, sound the death knell for virtually all Chapter 11 cases. In every case, the secured creditor could simply purchase either 51% in number or over one-third in amount of the unsecured claims and thereby be virtually assured of being able to block the confirmation of a cramdown plan by the debtor. This cannot be the result which Congress intended. Indeed, it is submitted that such activity is the very type of harm which Congress sought to empower and direct the Bankruptcy Courts to prevent when it enacted Section 1126(e).

Contrary to Respondent's assertions, the Ninth Circuit Opinion will result in a "free for all" whereby a secured creditor will attempt, as in the case at bar, to buy as many claims as possible to obtain a blocking position ***before*** any plan has been proposed and ***before*** any Court-approved disclosure statement has been transmitted to creditors so that they have adequate information prior to determining whether to sell their claims, all in contravention of the disclosure and solicitation provisions of the Code. A secured creditor can acquire its blocking position without adhering to the strictures of Section 1125. This would upset the "delicate balance" enacted by Congress (and alluded to by Respondent) as set forth in Sections 1125 (providing for a Court-approved disclosure statement to be used in soliciting acceptances of a plan), 1126 (setting forth voting procedures on a plan) and 1129 (setting forth confirmation requirements) of the Code. The designation of the claims purchased by Respondent as nonvoting will preserve the primary purpose of Chapter 11 and prevent the type of abuse by secured creditors in Chapter 11 cases in which Respondent has engaged.

Indeed, Respondent's tactic in purchasing claims to block confirmation of a debtor's plan is not and cannot be an isolated case. It would be a rare debtor, however, which would have the resources and opportunity to seek review by this Court of the pernicious conduct engaged in here. The

fact that such claims trading may result in blocking the successful reorganization of a Chapter 11 debtor does not mean that such conduct and its adverse consequences to the purposes and policies underlying the Code should be insulated from review by this Court. This case provides the opportunity for the Court to undertake such review.

As discussed, the Ninth Circuit Opinion adversely affects all Chapter 11 cases. Single-asset debtors, such as the Petitioner, however, are particularly susceptible and vulnerable to a secured creditor engaging in claims purchasing because such debtors typically have only one single, secured creditor and a number of unsecured trade creditors. The sole secured creditor in such a situation may more easily acquire a blocking position. This adverse impact on single-asset debtors also warrants review of the Ninth Circuit Opinion by this Court.

As discussed in the Petition (at 11-12), the Code was most recently amended by Congress in 1994. Pub. L. 103-94, 108 Stat. 4106 (1994). Significantly, as noted by various commentators, the 1994 amendments did ***not*** bar single-asset debtors from seeking Federal bankruptcy protection. If Congress had intended that single asset debtors would not be entitled to reorganize under Chapter 11, it could have done so by way of the 1994 amendments. It chose not to do so. Judicial interpretations of the Code, such as set forth in the Ninth Circuit Opinion, which render it difficult or impossible for a single asset real estate debtor such as the Petitioner to reorganize, are inconsistent with the purpose and policy of the Code and the intent of Congress.

The Ninth Circuit Opinion thus involves important Federal questions warranting review by this Court.

2. The Ninth Circuit Opinion Conflicts with Supreme Court Precedent.

Respondent's argument that *Pioneer Investment Services Co. v. Brunswick Assoc. LP*, 507 U.S. 380 (1993), is inapplicable to this case is without merit. Respondent concedes that the meaning of "good faith" for purposes of Section 1126(e) of the Bankruptcy Code was left undefined by Congress (Resp. Br. at 6). The Bankruptcy Courts are thus left with the discretion, in the exercise of their equitable powers, to interpret the meaning of such term. As the Petitioner stated in the Petition, in *Pioneer*, this Court stated that "bankruptcy courts are entrusted with broad equitable powers *to balance the interests of the affected parties, guided by the overriding goal of insuring the success of the reorganization.*" 507 U.S. at 389 (emphasis added). Although the Petitioner agrees with Respondent that the Bankruptcy Code need not be interpreted with a "debtor's green glasses," *Pioneer* does require that the Bankruptcy Courts "*balance the interests of the affected parties.*" *Id.* It would appear that, at the very least, *Pioneer* requires that, in the absence of the expression of any legislative intent to the contrary, in exercising their equitable powers in balancing such interests (for example in interpreting the provisions of the Code as Congress entrusted such Courts to do), the Bankruptcy Courts should err on the side of promoting a successful reorganization. In interpreting "good faith" under Section 1126(e) of the Code in a manner which renders it difficult, if not impossible, for the Petitioner to reorganize, the Ninth Circuit Opinion was clearly not guided by the "*overriding goal of insuring the success of the reorganization.*"

Also without merit is Respondent's argument that this Court's decision in *Young v. Higbee*, 324 U.S. 204 (1945), which interpreted the predecessor statute to Section 1126(e) of the Code (Section 203 of the Bankruptcy Act of 1898, 11 U.S.C. § 603), was ***only*** intended to apply to those whose

selfish purpose was "to obstruct a fair and feasible reorganization in the hope that someone would pay them more than the ratable equivalent of their proportionate part of the bankrupt assets." 324 U.S. at 210-211. In fact, various Federal courts, following *Young*, have found bad faith within the meaning of Section 1126(e) of the Code in a variety of circumstances and not just where the creditor obtained a plan blocking position for the limited purpose of obtaining more than its fair share of any distribution. *See, e.g., In re Applegate Property, Ltd.*, 133 B.R. 827 (Bankr. W.D. Tex. 1991) (votes of insiders disqualified who had purchased claims to prevent the proponent of a competing plan from purchasing them, because such conduct constituted an "obstructionist tactic done in contemplation of gaining an unfair advantage over other creditors" and because "such conduct cannot, as a matter of law, be in good faith"); *In re Allegheny International*, 118 B.R. 282 (Bankr. W.D. Pa. 1990) (acquisition of a blocking position was in bad faith because it was aimed at defeating the debtor's plan and was meant to obstruct a fair and reasonable organization); *In re Holly Knoll Partnership*, 167 B.R. 381, 388 (Bankr. E.D. Pa. 1994) (finding that the purchasing creditor was not acting to protect or maximize its rights as a creditor but, rather, was acting to preserve financial advantages it would receive if the plan was confirmed, enabling it to gain control of the debtor and to collect certain management and construction fees, the Bankruptcy Court disallowed such creditor's vote as not being in good faith).

Here, Respondent ***has admitted*** that the purpose of its claims purchases was to ***block confirmation*** of Figter's proposed plan of reorganization. In doing so, Respondent hoped to gain a preferential advantage over the other creditors. This is precisely the kind of behavior which this Court found constituted bad faith in *Young*, *supra*, 324 U.S. at 210-211. Furthermore, Respondent did, in fact, intend to obtain more that its ratable share of the bankruptcy estate. Respondent had, as ulterior motives in purchasing the claims,

the intent to, among other things, (1) foreclose on and thereby garner the equity in Figter's real property for itself; and (2) hamper Figter's ability and incentive to continue the pending adversary proceeding against Respondent. Moreover, as discussed in the Petition, Respondent was not simply attempting to act in good faith to advance what it reasonably has determined to be its best interests as a creditor in this case. Respondent purchased claims ***outside*** the secured class to which it belonged. (Petition at 19-20). The Ninth Circuit Opinion, however, refused to apply the holding of this Court's decision in *Young*, *supra*, that a selfish purpose to ***obstruct a fair and feasible reorganization*** constitutes bad faith, resulting in denial of the right to vote on a plan. If this Court's precedent had been followed and applied by the Court of Appeals, a finding of bad faith should have been made.

The Ninth Circuit Opinion is also in conflict with precedents of this Court on the issue of whether Respondent, if the claims it purchased are not designated as nonvoting, should have been found entitled to only one vote with respect to the claims it purchased. As discussed in the Petition, in a variety of pre-Code contexts, the assignee or holder of multiple claims in the same class has only one vote for purposes of voting in a bankruptcy proceeding. (Petition at 24-25). In *Dewsnup v. Timm*, 502 U.S. 410, 419-420 (1992), this Court held that, unless there is a discussion to the contrary in the legislative history, the Code is not to be construed as intending "to effect a major change in pre-Code practice." The Court of Appeals, however, effected a "major change in pre-Code practice," by rejecting analogous bankruptcy precedent in the context of the predecessor statutes to Chapter 11 of the Code without any reference to any legislative history which might justify such a departure.

Because of these conflicts with precedents of this Court alone, the Petition should be granted. Under the totality of the circumstances in this case, Respondent did not act with

proper motive or in a proper manner in its claims purchases and otherwise acted in bad faith. In finding otherwise, the Court of Appeals and the courts below have ignored the dictates of this Court that they must have as an ***overriding*** goal, insuring the success of the reorganization. The decisions below jeopardize the successful reorganization of not only the Petitioner but all Chapter 11 debtors and are contrary to the teachings of this Court, the purposes of the Code and the intent of Congress. The Petition should be granted so that the Court may exercise its supervisory power to correct this departure from applicable precedent and legislative intent.

3. Respondent Is in Any Event Entitled to Only One Vote for Each of the Unsecured Claims Purchased.

Contrary to Respondent's argument, the plain language of Section 1126(c) of the Code does not give a creditor a right to vote multiple claims and does not bar any inquiry into pre-Code case law. The Petition (at 24-28) cited the historical rule, analogous pre-Code cases and excerpts from the *Colliers* treatises, all of which demonstrate that multiple purchased claims should be tallied as one vote. The language of the Section 12 of the Bankruptcy Act and Section 1126(c) are virtually identical. Section 1126(c) does *not* expressly address the issue of the voting of multiple purchased claims. Neither the statute nor the legislative history contains any reference to or discussion of this issue. Therefore, Section 1126(c) does not contain "plain language" which sufficiently expresses a clear intent to change pre-Code practice. A Court reviewing the issue must accordingly conduct an inquiry into pre-Code cases and Congressional intent.

The Petitioner and Respondent both cite *Dewsnup v. Timm*, *supra*, but for different propositions. Respondent

cites *Dewsnup* for the proposition that the language of Section 1126(c) is unambiguous and any judicial inquiry should end there. (Resp. Br. at 10). The Petitioner cites *Dewsnup* for the proposition that the Code was not written on a completely "clean slate," nor enacted in a statutory vacuum. 502 U.S. at 419-420 (Petition at 26-27). To interpret the Code in a vacuum is not only counter-intuitive, but it also flies in the face of a long line of jurisprudence which cautions the Courts against an approach which ignores precedent and the statutory frameworks which existed prior to the enactment of the Code. *Dewsnup* holds that, unless there is a discussion to the contrary in the legislative history, the Code is not to be construed as intending "to effect a major change in pre-Code practice." *Id. See also Pennsylvania Public Welfare Dept. v. Davenport*, 495 U.S. 552, 563 (1990) (the Code should not be read to abandon past bankruptcy practices absent a clear Congressional intent to do so).

Even though Section 1126(c) refers to allowed "claims," that Section simply does not attempt to address how claims should be counted in the context of claims trading or where a creditor buys multiple claims which, through the sale process, have lost any independent basis by being aggregated by one party. Despite this, the Courts below effected a "major change in pre-Code practice," without any reference to any legislative history which might justify such a departure. To be consistent with *Dewsnup*, there would have to be a much clearer indication of intent by Congress to abrogate the prior case law and statutory rules which governed voting in a variety of previous statutory contexts. (Petition at 27). The "plain language" rule simply cannot be applied to Section 1126(c), which is completely devoid of any language regarding vote counting of multiple purchased claims. The Courts below nevertheless adopted broad new rules of voting, simply on the basis of the use of the word "claims" in Section 1126(c), as opposed to the words "claimants" or "creditors." Under applicable precedents of this Court, this is not enough to effect a major change in pre-Code practice.

Therefore, the Petition for Writ of Certiorari should be granted to determine whether the Ninth Circuit correctly ignored and disregarded prior precedents, under predecessor statutes, in a variety of analogous contexts, in refusing to find that Respondent is only entitled to one vote by virtue of the multiple unsecured claims which it holds.

CONCLUSION

This Court should grant certiorari to determine as a matter of law whether the claims purchases at issue were in bad faith within the meaning of Section 1126(e) of the Code or, alternatively, to determine that a purchaser of claims under the Code should be entitled to only one vote as to the claims it purchased.

DATED: November 7, 1997

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